

## Message Text

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ACTION EUR-25

INFO OCT-01 ISO-00 EURE-00 CIAE-00 PM-07 INR-11 L-03

ACDA-19 NSAE-00 PA-04 RSC-01 PRS-01 SP-03 USIA-15

TRSE-00 SAJ-01 DODE-00 EB-11 COME-00 FRB-03 SS-20

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DRC-01 /161 W

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P 301415Z JUL 74

FM USMISSION NATO

TO SECSTATE WASHDC PRIORITY 6961

AMEMBASSY MOSCOW

C O N F I D E N T I A L SECTION 1 OF 2 USNATO 4145

E.O. 11652: GDS

TAGS: ECON, EFIN, UR, NATO

SUBJECT: ECONADS: ESTIMATE OF SOVIET BALANCE OF PAYMENTS IN CONVERTIBLE CURRENCIES

REF: USNATO 3866

1. BELOW IS THE TEXT OF A DRAFT SUMMARY REPORT OF THE FINDINGS WHICH EMERGED FROM THE JULY 11 ECONOMIC COMMITTEE MEETING WITH EXPERTS ON THE SOVIET BALANCE OF PAYMENTS. REPORT IS ON AGENDA OF ECONADS MEETING AUG 1 FOR APPROVAL. MISSION WOULD APPRECIATE ANY ADDITIONAL COMMENTS US HAS ON REPORT BY COB JULY 31 TOGETHER WITH DATA US REP AGREED DURING MEETING TO SUPPLY (REFTEL).

2. BEGIN TEXT.

AN ESTIMATE OF THE SOVIET BALANCE OF PAYMENTS IN  
CONVERTIBLE CURRENCIES: PRINCIPAL FEATURES  
AND IMPLICATIONS

DRAFT SUMMARY REPORT TO THE COUNCIL  
CONFIDENTIAL

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THE FOLLOWING POINTS STEM FROM THE MAIN FINDINGS OF A  
PANEL OF EXPERTS FROM CAPITALS OF ALLIANCE COUNTRIES WHO  
CONSIDERED THE SUBJECT OF THE SOVIET BALANCE OF PAYMENTS IN  
HARD CURRENCIES AT A REINFORCED MEETING OF THE ECONOMIC

COMMITTEE ON 11TH JULY.

2. THE SOVIET INTERNATIONAL FINANCIAL POSITION HAS BEEN CONSIDERABLY REINFORCED BY THE RAPID RISES OF OIL AND COMMODITY PRICES THAT HAVE DOUBLED THE VALUE OF SOVIET EXPORTS. THE TROUBLE, HOWEVER, IS NOT EXPECTED TO ACHIEVE CONVERTIBILITY AS A CONSEQUENCE, SINCE THIS WOULD IMPLY A FREEDOM OF EXCHANGE IN CONTRADICTION WITH THE SOVIET STATE-TRADING SYSTEM. THE RECENT SIGNIFICANT SHIFT IN THE INTERNATIONAL TERMS OF TRADE HAS RELIEVED EAST-WEST TRADE OF A MAJOR CONSTRAINT (INSUFFICIENCY OF SOVIET EXPORT EARNINGS) AND HAS ACCORDINGLY EXPANDED THE SOVIET CAPACITY TO IMPORT WESTERN MACHINERY, MANUFACTURED GOODS AND GRAIN, IMPORTANT TO SOVIET ECONOMIC GROWTH; AND HAS REDUCED THE BURDEN OF SOVIET DEBT TO NATO AND OTHER INDUSTRIALISED WESTERN COUNTRIES.

3. THE EXPERTS RECOGNISED THAT SOVIET FAILURE TO PUBLISH COMPREHENSIVE PAYMENTS DATA HAS NOT ONLY COMPLICATED THE QUESTION OF SOVIET ACCESS TO CERTAIN INTERNATIONAL ECONOMIC ORGANIZATIONS BUT HAS ALSO OBSCURED INDIVIDUAL ITEMS IN THE BALANCE (E.G. GOVERNMENT SERVICES, OTHER "INVISIBLES", SOME CAPITAL FLOWS). THE EXPERTS CONCLUDED, HOWEVER, THAT IMPORTANT ELEMENTS ARE SUFFICIENTLY CLEAR TO PERMIT AN ESTIMATE OF THE GENERAL STRUCTURE OF THE SOVIET EXTERNAL BALANCE AND OF RECENT SIGNIFICANT CHANGES IN IT. IN THIS CONNECTION, THE PERIODIC REPORTS OF THE ECONOMIC COMMITTEE BASED ON NOTIFICATIONS OF CAPITALS CONCERNING SOVIET DRAWINGS AND REPAYMENTS OF EXPORT CREDITS HAVE BEEN OF CONSIDERABLE RELEVANCE AND ASSISTANCE.

4. RECENT DEVELOPMENTS. THE RECENT TURNABOUT IN SOVIET EXTERNAL ECONOMIC FORTUNES IS REFLECTED IN KEY ELEMENTS OF THE BALANCE OF PAYMENTS IN CONVERTIBLE CURRENCIES AS PROJECTED BY THE EXPERTS:

(\$ MILLION)

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1972    1973    1974 (ESTIMATED)

EXPORTS            PLUS 2,815 PLUS 4,805 PLUS 6,000 TO PLUS 8,000

IMPORTS            - 4,175 - 6,525 - 5,500 TO -7,500

TRADE BLANCE      - 1,360 - 1,720 PLUS 500

INVISIBLES (NET)   (PROBABLY SMALL DEFICIT)(A)

GOLD SALES        PLUS 300 PLUS 965 PLUS 900(B)

(A) GOVERNMENT SERVICES IN PARTICULAR AND INTEREST PAYMENTS ARE BELIEVED TO HAVE BEEN NET DEFICITS

(B) AT AN ANNUAL RATE: SALES THROUGH JUNE HAVE TOTALLED ABOUT  
\$450 MILLION

5. THE TRANSFORMATION OF THE LARGE TRADE DEFICIT OF 1972  
INTO A SURPLUS IN 1974 REFLECTS THE POSSIBILITY THAT SOVIET  
EXPORT PROCEEDS MAY RISE MORE THAN 100 PER CENT AS A CONSEQUENCE  
PRINCIPALLY OF PRICE INCREASES, E.G. FOR OIL. SOVIET EXPORTS MAY ALSO  
BE BOOSTED BY THE NEW CAPABILITY OF SOME MIDDLE EASTERN CLIENTS TO  
PURCHASE SOVIET ARMS FOR HARD CURRENCY. SIMILARLY, PROCEEDS FROM  
SOVIET SALES OF GOLD TRIPLED LAST YEAR MAINLY BECAUSE OF A RISE IN  
PRICE AND HAVE SO FAR BEEN MAINTAINED AT ABOUT THIS RATE IN 1974.  
IN VIEW OF THE CONSIDERABLE STRENGTH OF SOVIET EXTERNAL PAYMENTS,  
THE EXPERTS FELT THAT THE PROCEEDS FROM GOLD EXPORTS IN 1973  
EXCEEDED WHAT WAS REQUIRED TO ACHIEVE A BALANCE.

6. THIS IMPROVEMENT IN THE LIQUIDITY POSITION OF THE USSR  
WAS ACCOMPANIED BY A DOUBLING OF SOVIET IMPORTS FROM THE HARD-  
CURRENCY AREA DURING 1972-1973. IMPORTS ARE EXPECTED TO REMAIN  
AT A RELATIVELY HIGH LEVEL (AT LEAST \$5.5 BILLION) THIS YEAR,  
THOUGH THE ASSORTMENT MAY SHIFT SOMEWHAT FROM GRAIN TO EQUIPMENT  
AND TECHNOLOGY. NEW SOVIET ORDERS FOR WESTERN MACHINERY ARE  
CURRENTLY WELL AHEAD OF THE RECORD-BREAKING 1973 LEVEL IN TERMS  
OF ANNUAL RATES. THE SHARE OF NATO COUNTRIES IN SOVIET COMMERCE  
IN HARD CURRENCIES REMAINS PROMINENT, ACCOUNTING FOR OVER THREE-  
QUARTERS OF THE TRADE DEFICIT AND OVER TWO-THIRDS OF THE VALUE OF  
GOODS EXCHANGED IN 1973.  
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C O N F I D E N T I A L SECTION 2 OF 2 USNATO 4145

7. THE INCREASE IN EARNINGS OF SOVIET EXPORTS OF ENERGY AND MATERIALS HAS ALSO CONSIDERABLY RELIEVED THE DEBT BURDEN OF THE USSR. THE RATIO OF SOVIET DEBT SERVICE TO EXPORTS HAS REMAINED WELL BELOW 20 PER CENT - A PERCENTAGE CONSIDERED COMPATIBLE WITH CURRENT SOVIET FINANCIAL CAPABILITIES. THE ESCALATION OF GOLD PRICES IN THE PAST TWO YEARS HAS ALMOST QUADRUPLD THE BOOK VALUE OF THE SOVIET GOLD STOCK (WHICH IS VARIOUSLY ESTIMATED BETWEEN 1,700 TO 2,000 TONS). AT THIR CURRENT VALUATION (WELL OVER \$8 BILLION), SOVIET GOLD RESERVES ARE MORE THAN DOUBLE THE ENTIRE SOVIET DEBT (UNDER \$4 BILLION) TO NATO AND OTHER INDUSTRIAL WESTERN COUNTRIES RESULTING FROM DRAWING ON WESTERN EXPORT CREDITS. SOVIET RESERVES MAY NOW BE EQUIVALENT TO THE VALUE OF 12-15 MONTHS OF SOVIET IMPORTS IN CONVERTIBLE CURRENCIES; THE CORRESPONDING RATIO IN WESTERN EUROPE IS ONLY 3 TO 7 MONTHS.

8. IN THE VIEW OF SOME EXPERTS, THE USSR MAY BECOME A SUBSTANTIAL NET LENDER THIS YEAR IN THE EURO-MARKET, UTILISING FOREIGN EXCHANGE ACCUMULATED IN 1972-1973. ALREADY IN EVIDENCE IS AN INCREASED SOVIET TENDENCY TO PAY CASH FOR EXPENSIVE PURCHASES OF WESTERN PLANT AND EQUIPMENT THAT HAD FORMERLY BEEN OBTAINED ALMOST EXCLUSIVELY UNDER LONG-TERM CREDITS.  
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9. SOVIET BORROWING NEVERTHELESS CONTINUED TO RISE LAST YEAR, PROBABLY EXCEEDING \$1.7 BILLION IN DRAWINGS ON GUARANTEED AND NON-GUARANTEED EXPORT CREDITS. THE USSR ALSO REPORTEDLY BORROWED FROM THE EURO-MARKET. THE APPARENT SOVIET WILLINGNESS TO GO ON ACCUMULATING DEBT OBLIGATIONS AT A TIME OF STRONG LIQUIDITY MIGHT REFLECT A HOPE TO PROFIT BY DIFFERENTIALS IN INTEREST RATES. MOSCOW MAY GLADLY PAY THE RELATIVELY LOW RATES OF WESTERN EXPORT CREDITS IN RETURN FOR THE OPPORTUNITY TO CHANNEL FOREIGN EXCHANGE INTO THE EURO-MARKET FOR REPAYMENTS AND CONCEIVABLY ALSO FOR PURPOSES OF SHORT-TERM INVESTMENT AT HIGH RATES.

10. PROSPECTS. AFTER 1974, INCREASES IN THE VALUE OF SOVIET EXPORTS AND IMPORTS WILL PROBABLY SLOW DOWN TO A MORE MODERATE PACE UNLESS WORLD COMMODITY PRICES AGAIN RISE DRAMATICALLY. WHILE SUCH PRICE FLUCTUATIONS REMAIN UNPREDICTABLE, SOVIET EXPORT PROSPECTS ARE FAVOURABLE SINCE THE USSR IS A MAJOR REPOSITORY OF MINERALS IN AN ERA OF CONSIDERABLE UNCERTAINTY OR SCARCITY. MOREOVER, IN 1975 GOLD SALES MAY RISE AS HIGH AS (\$1,300 MILLION) AN INCREASE OF ABOUT \$400 MILLION) AT CURRENT PRICES; THE TONNAGE PRODUCED AND SOLD ABROAD BY THE USSR IS EXPECTED TO GROW IN VOLUME IN RESPONSE TO PAST INCREASES IN GOLD PRICES, WHICH ARE NOW BELIEVED TO EXCEED PRODUCTION COSTS IN THE USSR. MOREOVER, REPAYMENTS BY DEVELOPING COUNTRIES OF PAST SOVIET CREDITS COVERING MILITARY AID ARE EXPECTED TO RISE TO APPROXIMATELY \$600-750 MILLION IN HARD CURRENCIES IN 1975 FROM AN ESTIMATED \$250 MILLION IN 1973. THE EXPERTS NEVERTHELESS BELIEVED THAT THE USSR WOULD CONTINUE TO BE INTERESTED IN

WESTERN EXPORT CREDITS, ESPECIALLY THOSE ASSOCIATED WITH LARGE-SCALE, SELF-LIQUIDATING DEVELOPMENT PROJECTS WHERE REPAYMENT CAN BE MADE WITH GOODS.

11. IF - AS SEEMS LIKELY - WORLD PRICES OF THE PRINCIPAL EXPORTS OF THE USSR REMAIN HIGH, THE RESULTANT STRENGTHENING OF ITS RESERVES AND LIQUIDITY WILL SUSTAIN A WIDE SOVIET FREEDOM OF MANOEUVRE IN THE DIRECTION OF BOTH CONCESSION AND PRESSURE VIS-A-VIS EASTERN EUROPE AS WELL AS ITS WESTERN TRADING PARTNERS.

12. THE EXPERTS AGREED TO TRANSMIT, AT A LATER TIME, ADDITIONAL DATA THAT MIGHT FACILITATE MORE PRECISE ESTIMATES OF CONFIDENTIAL

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CAPITAL FLOWS IN THE SOVIET BALANCE OF PAYMENTS IN CONVERTIBLE CURRENCIES.

END TEXT.

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